

UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF SOUTH CAROLINA

FILED
at ___ O'clock & ___ min ___ M

SEP 11 2003

BRENDA K. ARGOE, CLERK
United States Bankruptcy Court
Columbia, South Carolina (33)

IN RE:

Jack Funderburk d/b/a
Southstar Equipment,

Debtor.

Robert F. Anderson, Trustee,

Plaintiff,

v.

Republic Western Insurance Company,

Defendants.

C/A No. 01-05395-W

Adv. Pro. No. 02-80335-W

ENTERED

SEP 11 2003

JUDGMENT

KPD

Chapter 7

The Court hereby enters judgment in favor of Republic Western Insurance Company in the above referenced matter and declares that the loss claimed by the Plaintiff is not covered by the insurance policy for the reasons set forth in the attached order.


UNITED STATES BANKRUPTCY JUDGE

Columbia, South Carolina
September 10, 2003.

UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF SOUTH CAROLINA

FILED

at ___ O'clock & ___ min ___ M

SEP 11 2003

BRENDA K. ARGOE, CLERK
United States Bankruptcy Court
Columbia, South Carolina (33)

IN RE:

Jack Funderburk d/b/a
Southstar Equipment,

Debtor.

Robert F. Anderson, Trustee,

Plaintiff,

v.

Republic Western Insurance Company,

Defendants.

C/A No. 01-05395-W

Adv. Pro. No. 02-80335-W

ENTERED

SEP 11 2003

ORDER

KPD

Chapter 7

This matter came before the Court on the Complaint filed by Robert F. Anderson, Trustee ("Plaintiff") against Republic Western Insurance Company ("Republic"). A trial was held before the Court on August 18, 2003. Based on the arguments of counsel, evidence submitted and the pleadings before the Court, the Court enters its order granting judgment in favor of Republic and denying the relief requested by the Plaintiff.

Findings of Fact

The parties stipulated to the following facts:

1. Jack Funderburk ("Debtor") operated an equipment rental business under the trade name South Star Equipment. The Debtor owned various pieces of equipment used for rentals in his business and financed some or all of the equipment through secured loans with various lenders. The Plaintiff has identified the Debtor's equipment in Plaintiff's Exhibit 1 which is Trustee's proof of claim with supporting documentation filed on January 17, 2002 in

the Sprint Auction Company of SC, Inc.¹ bankruptcy case; and Plaintiff's Exhibit 8.

2. The Debtor and Easler Auction Company, Inc. ("Easler") entered into an agreement (the "Auction Agreement") for a public auction of Debtor's equipment. The Debtor agreed to sell the equipment free and clear of liens or encumbrances. The Debtor delivered the equipment to Easler, and Easler conducted an auction in October 2000. Easler failed to remit the proceeds from the auction to the Debtor. The Debtor remained obligated to lenders secured by the equipment after the auction.

3. Easler filed a Chapter 11 bankruptcy case on or about May 4, 2001.

4. The Debtor filed a Chapter 11 bankruptcy case on May 24, 2001. The Debtor's Chapter 11 case was converted to a Chapter 7 case on August 14, 2001. The Plaintiff is the trustee for the Debtor's Chapter 7 case.

5. Prior to his bankruptcy case, the Debtor did not sue Easler for the recovery of the auction proceeds.

6. The Plaintiff filed a proof of claim for the amount of \$2,150,449.23 in the Easler bankruptcy case.

7. The Defendant, Republic Western Insurance Co. (hereafter "Republic"), issued an insurance policy to the Debtor effective for the period September 17, 1999 through September 17, 2000; and September 17, 2000 to September 17, 2001. (the "Policy").

8. On June 19, 2002, the Plaintiff made a demand on Republic to pay the loss arising out of the auction; Republic denied coverage for the loss by letter dated July 23, 2002. The June 19, 2002 letter was the first notice given to Republic regarding the claimed loss.

¹ Sprint Auction Company of SC, Inc. is formerly known as Easler Auction Company.

On October 18, 2002, the Plaintiff commenced the adversary proceeding to determine an interest in and construction of the Policy and for turnover of property of the estate.

9. The proceeding is core pursuant to 28 U.S.C. §157(b)(2)(A) and (E).

10. Bob Faulkner, an accountant, was the only witness and testified that the Debtor was owed approximately \$1,259,446.97 from Easler. Mr. Faulkner also testified that Easler had remitted some of the auction proceeds either to the Debtor or directly to the Debtor's secured creditors.

The Policy and the Auction Agreement

11. The Policy provides that the following forms and endorsements are part of the Policy which apply to the claim made by the Plaintiff:

CP0090 (07/88), CP1030 (06/95), CP0030 (06/95), CP0110 (07/88), IL0194 (04/98)
CM0001 (06/95), CM7613 (04/93), CG7400 (04/92), CM7600 (04/92),
CP7200(04/92), IL8802 (04/92), IL0003 (11/85), IL0017 (11/98), IL0935 (08/98),
IL0249 (08/99),

See Exhibit 3, Pg. 3.²

12. The Policy provides:

This form insures against risks of direct physical loss or damage to property covered except as hereinafter provided.

...

13. The Policy also provides that:

This form insures all personal property owned by or for which the insured may be liable, but excludes:

....

2. Currency, money, stamps, bullion, notes, securities, deeds, accounts, bills, evidences of debt, letter of credit, and tickets; credit cards.

....

4. Motor vehicles, meaning any land vehicle (excluding any machinery

² All references to the Policy refer to the Policy submitted as Plaintiff's Exhibit 3 and the page numbers included therein.

or apparatus attached thereto) which is self-propelled and designed or planned for highway use as a means of transportation; aircraft.

Exhibit 3, Pg. 7.

14. The Policy provides that:

This form does not insure against:

....

8. Any fraudulent, dishonest or criminal act done by or at the instigation of any insured, partner or joint adventurer in or of any insured; an officer, director, or trustee of any insured; or any fraudulent, dishonest or criminal act of any employee while working or otherwise.

Exhibit 3, Pg. 8.

15. The Policy provides under Exclusions in the Causes of Loss – Special Form that:

We will not pay for loss or damage caused by or resulting from any of the following:

h. Dishonest or criminal act by you, any of your partners, employees (including leased employees), directors, trustees, authorized representatives or anyone to whom you entrust property for any purpose . . . This exclusion does not apply to acts of destruction by your employees (including leased employees); but theft by employees (including leased employees) is not covered.

i. Voluntary parting with any property by you or anyone else to whom you have entrusted the property if induced to do so by any fraudulent scheme, trick, device or false pretense.

16. The Policy also provides under Conditions that:

B. It is understood and agreed that each claim for loss or damage hereunder shall be adjusted separately and from the amount of each claim when determined the sum of the deductible shown on the declarations or the deposit obtained from the rentee, whichever is greater shall be deducted.

E. Recovery of property. Immediately upon discovery of the situation which may result in a claim hereunder, the insured agrees to exert all reasonable efforts (which shall be construed to mean taking any legal means which would normally be taken by a prudent uninsured interest) to reduce or eliminate such loss. Failure to exercise such prudent efforts shall invalidate any claim under this policy.

M. Conversion, or other dishonest act on part of any person(s) to whom, the insured property is entrusted, or any person(s) in service or employment of rentee (leasee) whether or not occurring during the hours of such service or employment.

17. The Policy provides that the deductible on claims is \$1,500.

18. The Auction Agreement between the parties provides that “Seller (defined in the contract as Southstar Equipment) hereby agrees to deliver said equipment to purchaser by Bill of Sale, free and clear of all liens and encumbrances.”

19. The Auction Agreement provides “Auctioneer agrees to make prompt and full payment of its debt to seller less auctioneer’s deduction for commission and charges, as stated in item #2, within twenty-one (21) working days of the auction sale, thus allowing Auctioneer ample time to clear checks given to auction company and to receive the full gross receipt in good negotiable U.S. currency.”

CONCLUSIONS OF LAW

Rules of Construction

The Plaintiff is seeking a declaratory judgment that the claimed loss is covered by the Policy. “A declaratory judgment action to interpret an insurance contract is an action at law.” Loadholt v. SC State Budget and Control Board, Div. of General Services, Ins. Reserve Fund, 528 S.E.2d 670, 672-673 (S.C. Ct. App. 2000). In interpreting an insurance contract, the general rules of contract construction are used. Thompson v. Continental Ins. Co., 351 S.E.2d 904 (S.C. Ct. App. 1986). If the contract terms are not uncertain, they should be read and given effect as reasonably intended by the parties. Id. “The rule of strict construction against the insurer does not apply where the language used in the policy is so plain and unambiguous as to leave no room for construction.” S.S. Newell & Company v. American Mutual Liability Ins. Co., 19 S.E.2d 463, 466 (S.C. 1942). The South Carolina Supreme Court has held:

We must enforce, not write, contracts of insurance and we must give policy language its plain, ordinary and popular meaning. We should not torture the meaning of policy language in order to extend or defeat coverage that was never intended by the parties.

Gambrell v. Travelers Ins. Co., 310 S.E.2d 814, 816 (SC 1983). “Exclusions in an insurance policy are to be read independently of each other; they are not to be read cumulatively.” Engineered Products, Inc. v. Aetna Casualty & Surety Company, 368 S.E.2d 674, 675 (S.C. Ct. App. 1988). The insured has the initial burden of showing that the claimed loss is covered by the Policy. If the insured meets this burden, then the burden shifts to the insurer to show that an exclusion under the Policy applies.

A. The Loss is Not Covered by The Policy

The Policy provides that it “insures against risks of direct physical loss or damage.”³ The Plaintiff asserts that the loss for which it seeks recovery is the loss of the equipment from the auction. The Debtor claims that it suffered a loss because the Debtor remained liable on the debts which were secured by the equipment. As such, the Plaintiff states that the loss of the equipment is covered by the Policy. The Plaintiff has cited the cases of Benton & Rhodes, Inc. v. Boden, 426 S.E.2d 823 (S.C. Ct. App. 1993), and Reid v. Hardware Mutual Ins. Co. of Carolinas, 166 S.E.2d 317 (S.C. 1969) for the proposition that the Debtor had an insurable interest in the equipment which is covered by the Policy. In Benton & Rhodes, Inc. and Reid, the insured sold property to a third party who was aware of, or had assumed liens, which encumbered the property. After the sales, the property was destroyed by fire. In both cases, the South Carolina courts found that the insured had an insurable interest in the property which was covered by the insurance policy.

The Court does not need to reach the issue of whether the Debtor maintained an insurable

³ See Plaintiff’s Exhibit 3, the Policy, at page 7.

interest in the equipment following the auction. If the loss of the equipment is not covered by the Policy, then the Debtor's insurable interest is moot. Unlike the cases cited by the Plaintiff, the Plaintiff is claiming that the loss is that it no longer has possession of the equipment and is still liable on the debts which encumbered the equipment. Neither Benton & Rhodes, Inc. or Reid stand for the proposition that the transfer of ownership to a third party purchaser results in a loss within the meaning of an insurance policy. Rather those cases stand for the proposition that the seller had an insurable interest in property which was subsequently lost to fire. The Debtor's loss of possession of the equipment is not a covered loss within the plain meaning of the Policy. To interpret the meaning of loss to include property which was voluntarily sold by the Debtor would be a tortuous interpretation of the Policy in an effort to expand its coverage in a manner which was not intended by the parties to the Policy.⁴

Based upon the facts and evidence before the Court, the Court finds that the loss which was incurred by the Debtor was the failure to receive proceeds of the auction from the auctioneer. The insured property (the equipment) was turned over voluntarily to be sold, and it was sold. The proceeds from the sale of the equipment are separate and distinct from the equipment itself. See generally U.S. v. Lawson, 925 F.2d 1207 (9th Cir. 1991) (where auctioneer failed to turnover proceeds of auction, auctioneer may have converted proceeds not the actual property); State v. White, 137 S.E.2d 97 (S.C. 1964) (indictment for failure to remit proceeds when entrusted to sell

⁴ The Plaintiff is also not entitled to claim the loss of the equipment is covered, because the Plaintiff stands in the shoes of the Debtor at the time of the bankruptcy case. When the Debtor filed his bankruptcy petition, the Debtor had waived any interest he had in the equipment. The Debtor specifically agreed in the Auction Agreement that he was selling the equipment free and clear of all liens or encumbrances (which had to include his own interests as well). Additionally, S.C. Code Ann. § 36-2-328 provides in relevant part that a sale by an auction is complete when the auctioneer so announces by the fall of the hammer. Therefore, the Debtor waived any remaining interest he had in the equipment.

goods should be cite misappropriation of proceeds from sale rather than misappropriation of goods). Therefore, the actions of the auctioneer regarding the equipment were consistent with the request of the Debtor and did not result in a loss. There was no direct, physical loss to the equipment covered by the Policy. The subsequent action of the auctioneer in failing to turn over the money derived from the sale gave rise to the loss suffered by the Debtor.⁵ The Court finds that this loss was not one intended by the parties to be covered by the Policy.

To the extent that the Plaintiff might assert some special interest in the money from the sale of the equipment in an effort to argue that the loss is covered by the Policy, the Plaintiff had the burden to show that it held such a special interest in the auction proceeds (i.e., escrowed funds or held in trust). However, the facts in this case reflect that there was no special treatment provided for the funds. The Auction Agreement provides that the auction company owes the debtor “a debt” and does not require the creation or retention of any special fund. Courts in examining situations in which goods are sold have found that absent an agreement between the parties creating a special interest, a party is merely a creditor to the debtor for the funds due and owing. See, e.g., Rine & Rine Auctioneers, Inc. v. Douglas County Bank & Trust Co. (In re Rine & Rine Auctioneers, Inc.), 74 F.3d 854 (8th Cir. 1996); U.S. v. Lawson, 925 F.2d 1207 (9th Cir. 1991); Salem v. Lawrence Lynch Corp. (In re Farrell & Howard Auctioneers, Inc.), 172 B.R. 712 (Bankr. D. Mass. 1994). Therefore, the Debtor’s claim to the auction proceeds is no more than a debt owed by the auction company to it, and Plaintiff failed to show any special interest or entitlement to the money derived from the auction.

B. The Loss is Excluded from the Policy.

⁵ The Plaintiff acknowledges in his Complaint that the loss is due to the failure of Easler to remit proceeds from the sale of the Debtor’s equipment to the Debtor. See Complaint at ¶ 11.

As discussed above, the loss suffered by the Debtor was the auction company's failure to pay the debt it owed the Debtor. Even if Plaintiff had met his burden of proving a special interest in the money derived from the auction, an exclusion applies. The Policy clearly excludes such losses in the following language:

This form insures all personal property owned by or for which the insured may be liable, but excludes:

....

2. **Currency, money**, stamps, bullion, notes, securities, deeds, accounts, bills, **evidences of debt**, letter of credit, and tickets; credit cards.

See, Policy, Exhibit 3, Pg. 7 (emphasis added). Therefore, pursuant to the plain language of the Policy, the loss suffered by the Debtor is not covered. Money and evidences of debt are clearly and unambiguously excluded.

Republic also argued that the claimed loss would be excluded under the exclusions of dishonest or criminal conduct. The Court declines to infer from the facts that Easler acted dishonestly or criminally. However, the Court could reach the conclusion that the Debtor acted dishonestly by selling equipment free and clear of liens when he knew that the equipment was encumbered. The Debtor signed the Auction Agreement which specifically provided that the equipment was being sold free and clear of all liens. The evidence introduced by the Plaintiff clearly reflects that the equipment was under lien and that the Debtor was aware of the liens. Selling equipment under lien without revealing the existence of such liens is dishonest and may also be found to be a misdemeanor under South Carolina state law. However, as the Court has already determined that the Plaintiff has not met his burden of proving the existence of a covered loss and that even if he had a money exclusion applies, it finds no need to address the remaining arguments

made in this matter.⁶ Therefore, it is

ORDERED that the relief requested by the Plaintiff in his complaint is denied and judgment is entered in favor of Republic.

Columbia, South Carolina
September 10, 2003.


UNITED STATES BANKRUPTCY JUDGE

⁶ The Court notes that neither party cited to nor relied upon the Code of Laws of South Carolina regarding auctions and auctioneers. S.C. Code Ann. §§ 40-6-05 et seq. (Law. Co-op. 2001).